Supreme Court, U.S.
FILED
OCT 20 2000

(2)

No. 00-432

IN THE

Supreme Court of the United States

SALLY FRAME KASAKS, PAUL E. FRANCIS, JOSEPH R. GROMEK, ANNTAYLOR STORES CORPORATION and ANNTAYLOR, INC.,

Petitioners,

v.

CAROL NOVAK, ROBERT NEIMAN and JOSEPH DESENA, on behalf of themselves and all others similarly situated,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION

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Respondents Carol Novak, Robert Neiman and Joseph Desena, on behalf of themselves and all others similarly situated, submit this brief in opposition to the petition for a writ of certiorari filed by petitioners Sally Frame Kasaks, Paul E. Francis, Joseph R. Gromek, AnnTaylor Stores Corporation and AnnTaylor, Inc. For the reasons stated herein, the petition should be denied as to both questions presented, because neither question is properly presented for review in this case.

STATEMENT OF THE CASE

This is a securities class action brought by respondents Carol Novak, Robert Nieman and Joseph Desena on behalf of themselves and all other purchasers of the common stock of AnnTaylor Stores Corporation, a retailer of women's fashions, between February 3, 1994 and May 4, 1995 (the "Class Period").[1] Respondents allege that, throughout the Class Period, petitioners made materially false and misleading statements and omitted to state material facts concerning the financial performance of AnnTaylor, primarily by failing to account properly for millions of dollars of worthless and outdated merchandise inventories held by AnnTaylor in two secret warehouses. Respondents charged petitioners with violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78j(b) and 78t(a), and Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5.

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1. AnnTaylor Stores Corporation operates its business through its wholly-owned subsidiary, AnnTaylor, Inc. AnnTaylor Stores Corporation and AnnTaylor, Inc. are referred to collectively herein as "AnnTaylor" or the "Company."

Petitioners are AnnTaylor and certain senior officers of AnnTaylor during the Class Period.[2] Also named as defendants below were a group of Merrill Lynch affiliated entities and individuals who during the Class Period collectively sold over 42% of their own AnnTaylor stock for proceeds in excess of $155 million. Those defendants settled with respondents prior to the Second Circuit's decision and their sales of AnnTaylor stock were not considered by the Second Circuit and are not relevant to this petition.

A. The Facts as Alleged

Because this case concerns the disposition of a motion to dismiss filed by petitioners pursuant to Fed. R. Civ. P. 12(b)(6), all of the facts presented herein are based on the allegations of respondents' amended complaint.

Respondents allege that unbeknownst to the public, by the start of the Class Period (February 3, 1994), AnnTaylor had accumulated large amounts of excess merchandise inventories, which were beyond the levels internally budgeted or planned for by petitioners and which had not been marked-down and disposed of through the Company's stated markdown and factory store clearance process. Amended Complaint ¶¶ 30-45. To hide this serious problem from the marketplace and the investing public and to avoid large write-downs and liquidation

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2. The AnnTaylor officers named as defendants below are petitioners Sally Frame Kasaks ("Kasaks"), the Chairman of the Board, Chief Executive Officer and a director of AnnTaylor; Paul E. Francis ("Francis"), the Executive Vice President — Finance and Administration, Chief Financial Officer and a director of AnnTaylor; and Joseph R. Gromek ("Gromek"), the Senior Vice President — General Merchandise Manager of AnnTaylor. All of these individuals have since resigned from the Company.

of the excessive inventories, petitioners engaged in an elaborate scheme (which they internally called "Box & Hold"), by which millions of dollars of excessive and nearly worthless inventories were "Boxed" and "Held" in two secret warehouse locations throughout the Class Period. *Id.*

In violation of Generally Accepted Accounting Principles ("GAAP"), petitioners knowingly included the Box & Hold inventories at full value in AnnTaylor's publicly filed financial statements as part of AnnTaylor's reported gross inventory levels and as if they represented actual working inventory (which they did not), thereby artificially inflating AnnTaylor's reported profits and margins throughout the relevant time period. *Id.*[3]

Internal "Weekly Reports" distributed at regular Monday morning merchandise meetings identified the specific levels of inventory secretly held (without write-down) in Box & Hold, both in the aggregate and by product type and seasonal line. *Id.* Since petitioners Kasaks, Gromek and Francis each attended the regular Monday morning meetings and received the internal AnnTaylor Weekly Reports, which showed that the inventory held in and being added to Box & Hold could not and would not be disposed of without write-down and liquidation, they were each knowing participants in the fraudulent scheme,

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3. In their Statement of the Case, petitioners erroneously describe the fraudulent Box & Hold scheme alleged in the amended complaint as a "practice of storing certain unsold [AnnTaylor] inventory *for sale at a later time, typically when it was again in season*." Pet. 3 (emphasis added). In fact, as the Second Circuit recognized, respondents' complaint alleges that the Box & Hold inventory consisted of obsolete and nearly worthless inventory that had not been marked-down or disposed of as it should have been through petitioners' own publicly stated markdown policy. Pet. App. 4a, 23a.

through which petitioners deceived the investing public regarding AnnTaylor's financial performance and prospects, inventory, inventory controls, margins, net income and earnings per share. *Id.*

These executives are alleged to have known by February 2, 1994, the start of the Class Period, that $6 million of AnnTaylor's publicly reported inventory, or approximately 10% of the Company's total reported inventory at that time, consisted of the Box & Hold merchandise. *Id.* Thereafter, petitioners claimed throughout the Class Period that AnnTaylor's publicly reported inventory levels were growing to support the Company's expansion plans (or reflected the early arrival of holiday merchandise), when they knew that much of the growth in the Company's publicly reported inventory levels was due to the pile up of excess and obsolete inventory in Box & Hold, which, throughout the Class Period, was not removed from Box & Hold, disclosed to the public, written-down or liquidated. *Id.* At the end of the Class Period, there was a total of $32 million of inventory being held by the Company in Box & Hold, which was approximately 34% of AnnTaylor's total reported inventory as of January 28, 1995. *Id.*

At the regular Monday morning merchandise meetings and in other meetings throughout the Class Period, many AnnTaylor executives demanded that Kasaks, Francis and Gromek end the Box & Hold practice as it was growing out of control. *Id.* Petitioners' response to all of these demands was that AnnTaylor could not "afford" to eliminate, write-down or liquidate the Box & Hold inventory because doing so would "kill" the Company's reported financial results and profit margins, and damage the Company on "Wall Street." *Id.* In other words, each of these persons is alleged to have acted intentionally and deliberately to artificially inflate AnnTaylor's reported Class Period financial results with the Box & Hold scheme. *Id.*

B. Proceedings Below

Respondents brought suit on April 25, 1996, in the United States District Court for the Southern District of New York. Two years later, on March 10, 1998, the district court granted defendants' motions to dismiss, concluding that the complaint failed to satisfy the newly-enacted pleading requirements of the Private Securities Litigation Reform Act ("PSLRA"), 15 U.S.C. § 78u-4(b)(1), (2), because it did not plead with sufficient "particularity" facts supporting a strong inference that the defendants had acted fraudulently. Pet. App. 58a.

Respondents filed an amended complaint, but the district court dismissed that complaint as well on the same grounds. Pet. App. 39a. In its opinions, the district court faulted respondents for not specifically identifying documentary evidence of their claim and for not naming the former employees of AnnTaylor who were alleged to have substantiated the claim. Pet. App. 35a, 61a-62a.[4]

On appeal, following a *de novo* review of respondents' allegations, the Second Circuit vacated the district court's findings and remanded the action for further proceedings that are currently underway. The Second Circuit held that the district court erred in "(1) concluding that the [respondents] had failed to plead sufficient facts to support a strong inference of fraudulent intent; and (2) imposing an exceedingly onerous burden on the [respondents] with respect to their obligation to plead facts with particularity." Pet. App. 2a-3a. In so doing, the court of appeals undertook an extensive analysis of the statutory text and legislative history of the PSLRA and pre-existing Second Circuit case law.

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4. All discovery in this action was stayed by the district court as of August 16, 1996, during the pendency of defendants' motions to dismiss pursuant to 15 U.S.C. § 78u-4(b)(3)(B).

With respect to the requirements for pleading *scienter* set forth in section 78u-4(b)(2), the Second Circuit concluded that "Congress plainly sought to impose a stricter nationwide pleading standard," Pet. App. 21a, and that the new nationwide standard was largely equivalent to the pre-existing, strict Second Circuit *scienter* pleading requirements from which the PSLRA's "strong inference" language was incorporated (with Congress adding a "with particularity" requirement), Pet. App. 22a. The court held that, "[i]n order to plead *scienter*, [respondents] must 'state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind.' " Pet. App. 22a.[5] The Second Circuit found that respondents' amended complaint satisfied this newly enacted standard.

With regard to the requirement of pleading fraud "with particularity" set forth in 15 U.S.C. § 78u-4(b)(1), the court of appeals vacated the district court's findings because they were based "in substantial part" on the district court's erroneous conclusion that respondents were required as a matter of law to reveal the names of the confidential sources of their allegations in the complaint. Pet. App. 25a. The Second Circuit rejected any such requirement as a general matter. Pet. App. 28a-29a. Ultimately, the court of appeals did not "express [any] view as to whether [respondents'] allegations in this case were sufficiently particularized." Pet. App. 29a. Instead, it remanded the case

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5. Petitioners' reference to the *amicus* brief filed by the Securities and Exchange Commission in the Second Circuit below is misleading. *See* Pet. 5 n.2. In fact, the Second Circuit endorsed the position that the Securities and Exchange Commission and respondents had supported.

for the district court to "reconsider the particularity of [respondents'] pleadings in light of the proper standards." Pet. App. 30a.[6]

REASONS FOR DENYING THE WRIT

This case is an extraordinarily poor candidate for a grant of review by this Court, for three basic reasons.

First, the main conflict among the circuits identified by petitioners in their first question presented — disagreement over whether the *scienter* pleading provision of the PSLRA, 15 U.S.C. § 78u-4(b)(2), can be satisfied by pleading a defendant's "motive and opportunity" to commit fraud — is not relevant to the case as it now stands. The only allegations in this case based on "motive and opportunity" were those brought against the defendants affiliated with Merrill Lynch. Those defendants, however, settled before the Second Circuit's ruling. The case against the remaining defendants — petitioners — is based on specific facts alleged to show deliberate intent to defraud. *See* Pet. App. 23a. Accordingly, as petitioners concede, Pet. 13, the Second Circuit did not base its decision on any finding that allegations of "motive and opportunity" can suffice under the PSLRA. For that reason, this is not an appropriate case to address the alleged conflict among the circuits raised in petitioners' first question presented. If the Court were to grant review on that question, it would be reviewing general statements about the law that were never applied to the pleading at issue in this case.

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6. Petitioners are in error in claiming that the Second Circuit declared that it "could express no conclusion" as to whether the allegations of fraud in the amended complaint were sufficiently particularized." Pet. 5, 6, 14. It merely chose to remand for the district court to make this fact-specific determination.

As to the second question presented — the proper interpretation of the new requirement in the 15 U.S.C. § 78u-4(b)(1) that fraud be pled "with particularity" — petitioners gloss over a similar problem. Even if there is some tension between the Second Circuit's discussion of this issue and the Ninth Circuit's ruling in *In re Silicon Graphics Inc. Sec. Litig.*, 183 F.3d 970 (9th Cir. 1999) — and the true extent of any conflict is far from clear — the Second Circuit again did not apply its analysis to respondents' complaint. To the contrary, it "express[ed] no view" as to whether the complaint stated its allegations with sufficient particularity, Pet. App. 29a, and it remanded the case to the district court, where that matter currently is being litigated, Pet. App. 30a. It would make no sense whatsoever for the Court to review the Second Circuit's abstract and limited discussion of the "particularity" requirement, untethered to any application of the requirement to a particular pleading.

Finally, the legal issues presented in this action are relatively new and just beginning to be developed by the courts of appeal. Half the circuits have not even addressed the new requirements in the PSLRA for pleading *scienter*. Those that have done so all agree that recklessness, as defined by the Seventh Circuit in *Sundstrand Corp. v. Sun Chem. Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977), remains a sufficiently culpable state of mind following the passage of the new statute (except in certain limited circumstances in which proof of actual knowledge is now expressly required by the PSLRA) and that allegations of motive and opportunity to commit fraud are relevant and probative in analyzing allegations of *scienter* under this new statutory provision. All of these court of appeals decisions have been issued relatively recently — within the past sixteen months. Given time, the circuits are likely to harmonize their views

on this new pleading requirement and have the opportunity to address the newly-enacted pleading requirements of 15 U.S.C. § 78u-4(b)(1). Petitioners concede that other than the Second Circuit below, only one other circuit court decision has addressed the requirements of 15 U.S.C. § 78u-4(b)(1), and the extent of any disagreement between these two decisions is far from apparent. In sum, even if this were a good vehicle to address the meaning of the statute (which it is not), it would be premature for this Court to intervene.

I.

BECAUSE THE RELEVANT *SCIENTER* ALLEGATIONS IN THIS CASE WERE NOT BASED ON "MOTIVE AND OPPORTUNITY" TO COMMIT FRAUD, THIS IS NOT AN APPROPRIATE CASE IN WHICH TO ADDRESS THE FIRST QUESTION PRESENTED.

The primary conflict among the circuits identified by petitioners is whether the PSLRA, in section 78u-4(b)(2), mandates nationwide application of the pre-existing, stringent Second Circuit standard for pleading *scienter* in securities fraud cases or instead requires an even higher standard. *See* Pet. 9-10. Although that question was certainly considered and discussed by the Second Circuit, the issue is not really presented in this case, because nothing decided by the Second Circuit turns on the question.

As petitioners explain, the heart of the asserted conflict is whether section 78u-4(b)(2) requires modification of one aspect of the Second Circuit's pre-existing standard — allowing reliance in complaints on allegations of "motive and opportunity" to establish the requisite state of mind. *See* Pet. 10 (asserting that the Sixth, Ninth and Eleventh

Circuits have "held that the PSLRA established a more stringent pleading standard than the pre-existing Second Circuit standard, *most particularly by eliminating mere allegations of a motive and opportunity as a basis adequately to plead intent to commit securities fraud*") (emphasis added); *id.* (adding that the First Circuit also has disagreed with the Second Circuit about whether "mere allegations of motive and opportunity . . . adequately allege scienter"). The result in this case does not turn on that question in any way.

That is because respondents' *scienter* allegations against petitioners (as opposed to the other defendants who settled with plaintiffs prior to the Second Circuit's decision) were not based on claims of "motive and opportunity" to commit fraud. As the Second Circuit noted, "the Complaint alleges that the defendants engaged in conscious misstatements with the intent to deceive," Pet. App. 23a, and backs up that claim with specific allegations, having nothing to do with motive and opportunity, that constitute direct evidence of intentional fraud, *id.* As a result, petitioners concede that the motive and opportunity issue is not relevant to this case: "Because respondents did not allege that petitioners had a motive or opportunity to commit fraud, the Second Circuit's conclusion that the amended complaint below satisfied the requirements of the PSLRA was necessarily based on its allegations purporting to demonstrate 'strong circumstantial evidence of conscious misbehavior or recklessness.' " Pet. 13.

Accordingly, this is not an appropriate case in which to address the issue. The Court would be reviewing an abstract discussion with no relevance to the facts presented. Any ruling by the Court on question one would not make the

slightest difference in the posture in which this case was returned to the district court and would be tantamount to an advisory opinion.[7]

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7. Petitioners claim that the Second Circuit's interpretation of section 78u-4(b)(2) is in "direct conflict with Congress's unambiguously expressed intent," Pet. 11, but that argument disregards the fact that the Second Circuit — like nearly all of the other circuits to consider 15 U.S.C. § 78u-4(b)(2) to date — based its analysis on a review of the *plain language* of the statute. Pet. App. 20a ("In this case, our interpretive task begins and ends with the text of the statute."); *see Greebel v. FTP Software, Inc.*, 194 F.3d 185, 192-93 (1st Cir. 1999) (same); *In re Advanta Corp. Sec. Litig.*, 180 F.3d 525, 533-34 (3d Cir. 1999) (same); *In re Comshare, Inc. Sec. Litig.*, 183 F.3d 542, 549 (6th Cir. 1999) (same); *Bryant v. Avado Brands, Inc.*, 187 F.3d 1271, 1284 (11th Cir. 1999) (same).

Although petitioners would prefer the Court to focus on *one out-of-context portion* of the legislative history of the PSLRA, Pet. 12, nearly all of the courts of appeals to consider the PSLRA's legislative history have concluded that it is contradictory and inconclusive at best. *See, e.g.*, Pet. App. 21a ("the legislative history of the PSLRA contains 'conflicting expressions of legislative intent' with respect to the pleading requirements") (citation omitted); *Greebel*, 194 F.3d at 192 ("The legislative history is irretrievably conflicted. . . ."); *Advanta*, 180 F.3d at 533 ("Ultimately, we believe there is little to gain in attempting to reconcile the conflicting expressions of legislative intent. . . ."); *Comshare*, 183 F.3d at 552, n.10 ("Viewed in its entirety, the legislative history is ambiguous and does little to accurately reveal Congress' intent here.").

II.

BECAUSE THE SECOND CIRCUIT NEVER APPLIED THE "PARTICULARITY" REQUIREMENT TO THE FACTS OF THIS CASE, THIS CASE ALSO IS NOT AN APPROPRIATE ONE IN WHICH TO ADDRESS THE SECOND QUESTION PRESENTED.

For similar reasons, this would not be an appropriate case in which to address the meaning of section 78u-4b(1), requiring that when plaintiffs plead fraud on information and belief, they must "state with particularity all facts on which that belief is formed." In its opinion, the Second Circuit discussed this statutory requirement, but chose not to apply it to respondents' amended complaint, instead remanding for renewed consideration of the issue by the district court. The remand was necessary in the Second Circuit's opinion because the district court had concluded improperly that "plaintiffs had failed to meet these particularity requirements, in substantial part because they failed to reveal their confidential sources for some of the facts." Pet. App. 25a. The Second Circuit rejected any such requirement as a general matter and found that the two district court decisions that endorsed that approach did so "based on a misreading of the legislative history of the PSLRA." Pet. App. 27a-28a. With that guidance, the Second Circuit remanded this case to the district court for further proceedings to address whether or not the amended complaint was sufficiently particularized to comply with the requirements of the PSLRA. Those issues are just now being addressed by the trial court and remain unresolved. Again, therefore, the Court would be reviewing an abstract discussion of a legal standard that the court of appeals never applied to a concrete case. Given this situation, a grant of certiorari would be totally unwarranted. In addition

to the usual considerations counseling against a grant of review prior to entry of a final judgment in a case,[8] the Court's review in this case would be further hampered by the absence of *any* sort of *dispositive* ruling by the court of appeals.

Moreover, any conflicts between the Second Circuit's discussion of section 78u-4b(1) and the Ninth Circuit's discussion of the issue in *Silicon Graphics* are greatly exaggerated by petitioners. *See, e.g., In re McKesson HBOC, Inc. Sec. Litig.*, No. C-99-20743-RMW, 2000 U.S. Dist. LEXIS 14822, at *71 (N.D. Cal. Sept. 28, 2000) (finding "no conflict" between the Second Circuit's discussion of section 78u-4b(1) in this case and the Ninth Circuit's opinion in *Silicon Graphics* "which did not even address the issue" of confidential sources).

In this case, the Second Circuit ruled that the statutory requirement of pleading "all facts" supporting allegations of fraud does not mean that each and every detail must be included and specifically does not require revelation of confidential sources. Pet. App. 26a-28a. It reasoned that Congress cannot have meant to require inclusion of every single fact known to the plaintiffs, as long as sufficient facts are included to support their belief in the claim of fraud. Pet. App. 28a. The court also noted that "even if personal sources must be identified, there is no requirement that they be named, provided they are described with sufficient particularity to support the probability that a

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8. *See, e.g., Virginia Military Inst. v. United States*, 508 U.S. 946 (1993) ("We generally await final judgment in the lower courts before exercising our certiorari jurisdiction."); *Brotherhood of Locomotive Fireman & Enginemen v. Bangor & Aroostook R.R. Co.*, 389 U.S. 327, 328 (1967) ("Petitioners seek certiorari to review the adverse rulings made by the Court of Appeals. However, because the Court of Appeals remanded the case, it is not yet ripe for review by this Court. The petition for a writ of certiorari is denied.").

person in the position occupied by the source would possess the information alleged." Pet. App. 28a-29a.[9]

The Ninth Circuit, in turn, recited the statutory requirement of pleading "all the relevant facts forming the basis of [the plaintiff's] belief" in her fraud allegations. *Silicon Graphics*, 183 F.3d at 985. But it also seemed to indicate that it did not read this requirement literally. In discussing the company reports on which the complaint was based, the court faulted the plaintiff for not giving an "adequate description" of their contents, which would include "countless specifics" regarding the relevant circumstances. *Id.* But the court did not require inclusion in the complaint of *all* of these "countless specifics," stating instead that a "proper complaint . . . would contain *at least some* specifics from those reports as well as such facts as may indicate their reliability." *Id.* (emphasis added). Finally, although the Ninth Circuit also faulted the plaintiff for not "mention[ing] . . . the sources of her information with respect to the reports,"

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9. Petitioners' claim that the Second Circuit ignored the plain language of the PSLRA and its legislative history, Pet. 15-18, in holding that as a general matter confidential sources need not be disclosed in a pleading is misplaced. The Second Circuit's holding was based on its review of the statute's legislative history and, more importantly, the plain language of the statute as finally enacted:

> Specifically, the [district] court in *Silicon Graphics* relied primarily on the hyperbolic statements of legislators attempting (unsuccessfully) to amend the proposed Act to lighten plaintiffs' pleading burden. In fact, *the applicable provision of the law as ultimately enacted* requires plaintiffs to plead only facts and makes no mention of the sources of these facts.

Pet. App. 28a (emphasis added, citations omitted).

id., it did not make address whether revelation of confidential sources is always required and, if so, whether names or mere descriptions are sufficient.[10]

Thus, there is far from a compelling need for this Court to consider the issue presented in question two. Petitioners have pointed to only two circuit court cases discussing the question, and it is far from clear how much they diverge from one another. But the more important point is that this case's current posture effectively precludes meaningful consideration of the second question, because the court of appeals never applied the legal standards it was enunciating.[11]

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10. Petitioners' argument that the Second Circuit's decision is expressly in conflict with the Ninth Circuit's *Silicon Graphics* decision regarding the disclosure of confidential sources, Pet. 18, is erroneous. The decision below distinguished the *district* court's holding in *In re Silicon Graphics Inc. Sec. Litig.*, 970 F. Supp. 746, 763 (N.D. Cal. 1997) (which required the disclosure of confidential sources) and not the Ninth Circuit majority in *Silicon Graphics*, 183 F.3d at 984-85 (which simply noted that the plaintiff could have, but did not, provide, *inter alia*, sources to corroborate her allegations). *See* Pet. App. 27a.

11. Petitioners' other claim of error, that the Second Circuit only "paid lip service" to the PSLRA's newly enacted particularity requirements and applied section 78u-4(b)(2) in "such a manner as to write out of the statute the express requirement that fraudulent intent be pleaded 'with particularity,' " Pet. 9 n.3, 13-14, is in error. The Second Circuit found that there was "no doubt" that the amended complaint in this case satisfied "the requirement of the PSLRA that plaintiffs state facts *with particularity* that give rise to a strong inference of the required state of mind." Pet. App. 23a-24a (emphasis added). The fact that the Second Circuit remanded this action to the

(Cont'd)

III.

THE LEGAL ISSUES RAISED BY PETITIONERS ARE RELATIVELY NEW AND FURTHER DEVELOPMENT BY THE COURTS OF APPEAL IS APPROPRIATE.

Even if this case were a proper vehicle for addressing either of the questions presented by petitioners, a grant of review still would be highly premature. At this time, six circuits have not even addressed the newly enacted *scienter* pleading requirements of the PSLRA assertedly at issue in the first question presented by petitioners. Moreover, the circuits that have done so have agreed on much. They have all agreed, for example, that recklessness, as defined by the Seventh Circuit in *Sundstrand*, 553 F.2d at 1045, remains a sufficiently culpable state of mind following the passage of the new statute (except in certain limited circumstances in which proof of actual knowledge is now expressly required

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(Cont'd)
district court for further consideration of the particularity requirement of section 78u-4(b)(1) does not serve to show that the court of appeals ignored the particularity requirement of section 78u-4(b)(2) or provided a more lenient particularity standard for section 78u-4(b)(2). The Second Circuit's analysis merely demonstrates that the requirements of particularity in these two new statutory provisions may be analyzed separately. The Second Circuit's subsequent analysis in *Rothman v. Gregor*, 220 F.3d 81, 90 (2d Cir. 2000), does not hold otherwise. Rather, in *Rothman*, the court of appeals noted that particularity under sections 78u-4(b)(1), (2) could be analyzed together, but it did not express any requirement that they must be treated as co-extensive. *Id.* As set forth above, the sufficiency of the complaint's particularity under section 78u-4(b)(1) in this case is just being addressed by the trial court and remains unresolved at this time.

by the PSLRA).[12] They also have agreed that allegations of motive and opportunity to commit fraud are at least relevant and probative in analyzing allegations of *scienter* under this new statutory provision.[13]

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12. In this case, the Second Circuit reaffirmed its definition of recklessness set forth in *Rolf v. Blyth, Eastman Dillion & Co., Inc.*, 570 F.2d 38, 47 (2d Cir. 1978) (defining recklessness as "highly unreasonable" conduct that represents "an extreme departure from the standards of ordinary care"). *See* Pet. App. 15a. Each of the other courts of appeal that have interpreted the PSLRA has found that this same form of recklessness remains sufficient under the new statute. *See Greebel*, 194 F.3d at 198-200 (following *Sundstrand*, which articulated the same recklessness definition as *Rolf*); *Advanta*, 180 F.3d at 535 (same); *Comshare*, 183 F.3d at 550 (same); *Silicon Graphics*, 183 F.3d at 976 (same); *Howard v. Everex Sys., Inc.*, No. 98-17329, 2000 U.S. App. LEXIS 23973, at *17-18 (9th Cir. Sept. 29, 2000) (same); *Bryant*, 187 F.3d at 1284 n.21 (same). Certain of these courts of appeal have used different terms or labels to identify the *Sundstrand* standard, not to alter the *Sundstrand* standard, but to distinguish it from mere negligence. *See, e.g., Bryant*, 187 F.3d at 1284 (labeling the *Sundstrand* standard as "severe recklessness" and noting that it "does not allow for recklessness as a form of negligence"); *Silicon Graphics*, 183 F.3d at 976-77 (expressly adopting the *Sundstrand* standard, but describing it as "deliberate recklessness"). *See also Greebel*, 194 F.3d at 199; *Comshare*, 183 F.3d at 550.

13. *See* Pet. App. 22a; *Greebel*, 194 F.3d at 197 (rejecting defendants' argument that allegations showing motive and opportunity "can never be enough to permit the drawing of a strong inference of scienter"); *Advanta*, 180 F.3d at 535; *Comshare*, 183 F.3d at 551 (allegations regarding motive and opportunity may be "relevant to pleading circumstances from which a strong inference of fraudulent *scienter* may be inferred" and "may, on occasion, rise to the level of creating a strong inference of reckless or knowing conduct") (citation omitted); *Silicon Graphics*, 183 F.3d at 986 ("'unusual' or 'suspicious' stock sales by corporate insiders may constitute circumstantial evidence

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While all of these circuits have cautioned that bare allegations of motive and opportunity to commit fraud (regardless of the strength of the inferences to be drawn from those allegations) cannot be sufficient to satisfy section 78u-4(b)(2) (*see, e.g., Greebel*, 194 F.3d at 197; *Advanta*, 180 F.3d at 535; *Comshare*, 183 F.3d at 551; *Silicon Graphics*, 183 F.3d at 986; *Bryant*, 187 F.3d at 1285-86), the Second Circuit's analysis in this case is completely consistent with these holdings. Indeed, while finding its prior case law "helpful," Pet. App. 22a, the Second Circuit expressly cautioned in its decision that "litigants and lower courts need and should not employ or rely on magic words such as 'motive and opportunity,'" *id.*

Similarly, with respect to the particularity requirement of section 78u-4(b)(1), petitioners have cited only two circuit court opinions, and, as noted above, it is far from clear how much they diverge from one another.

None of these cases is older than sixteen months. Given time, the circuits will have the opportunity to further harmonize their views, given that their analyses are not as diverse or inconsistent as presented by petitioners. *See, e.g., Brown v. Texas*, 522 U.S. 940 (1997) (Stevens, J.) (writing on denial of certiorari that "the likelihood that the issue will be resolved correctly may increase if this Court allows other tribunals 'to serve as laboratories in which the issue receives further study before it is addressed by this Court' ") (citation omitted). It would make sense to allow that process to go forward.

(Cont'd)

of scienter"); *Howard*, 2000 U.S. App. LEXIS 23973, at *17-18 (same); *Bryant*, 187 F.3d at 1285-86 (allegations of motive and opportunity may be relevant to a showing of recklessness).

Certainly there is no basis for petitioners' claims that the Second Circuit has willfully defied Congress, *see* notes 7 and 9, *supra*, or that conflicts among the circuits are so deep and entrenched that they will lead to rampant forum shopping. Pet. 11, 19-22. In fact, given the current state of the law, no one could reasonably argue that any given complaint would fail as a matter of law in one circuit but would be sustained in another. There is thus no reason whatsoever to preempt the circuits' further consideration and elaboration of the issues presented in the petition.

CONCLUSION

For the foregoing reasons, respondents submit that the petition should be denied.

Respectfully submitted,

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